Oudtshoorn Municipality

Long Term Financial Plan – *Update February 2017*

Prepared by
INCA Portfolio Managers
February 2017

REPORT OVERVIEW – INTRODUCTION AND BACKGROUND

The Oudtshoorn Municipality appointed INCA Portfolio Managers in 2016 to prepare a Long Term Financial Plan. The deliverable of that assignment was a report entitled *Oudtshoorn Municipality; Long Term Financial Plan: 2016/17 – 2025/26*; July 2016. The estimates in that Plan will be referred to as the 2015 Estimate as they were based on the FYE2015 Annual Financial Statements. The Plan was updated with the latest available information in February 2017 (2016 Estimate).

The **objective of the Plan** was to recommend strategies and policies that will maximise the probability of the municipality's financial sustainability into the future. This is achieved by predicting future cash flows and affordable capital expenditure based on the municipality's historic performance and the environment in which it operates.

This February 2017 Update (2016 Estimate) aims to review the conclusions reached in 2016 based on the latest available information and report on the findings. A summary of the demographic-, economic- and household infrastructure perspective was updated with the latest available information as published by iHS Global Insight. The historic financial analysis was updated with the information captured in the municipality's unaudited financial statements of 30 June 2016. INCA Portfolio Managers' Capital Investment Model was populated and run with this latest information, and the outcome thereof is reported herein. In particular the capital budget assumptions and funding mix assumed by the municipality for the 3 years from 2016/17 to 2018/19 was assessed in the revision of the model.

Unlike the original assignment, no renewed analysis of the Asset Register, review of municipal documents (viz. Master Plans) and conversations with management were undertaken. The conclusions reached in this report are complimentary to the recommendations made previously.

The contents of this report entail the following:

1	Planning Process
2	Updated Perspectives (Demographic, Economic, Household Infrastructure)
3	Updated Historic Financial Assessment
4	Future Revenues
5	Affordable Future Capital Investment
6	Scenario Analysis
7	Ratio Analysis
8	Conclusions

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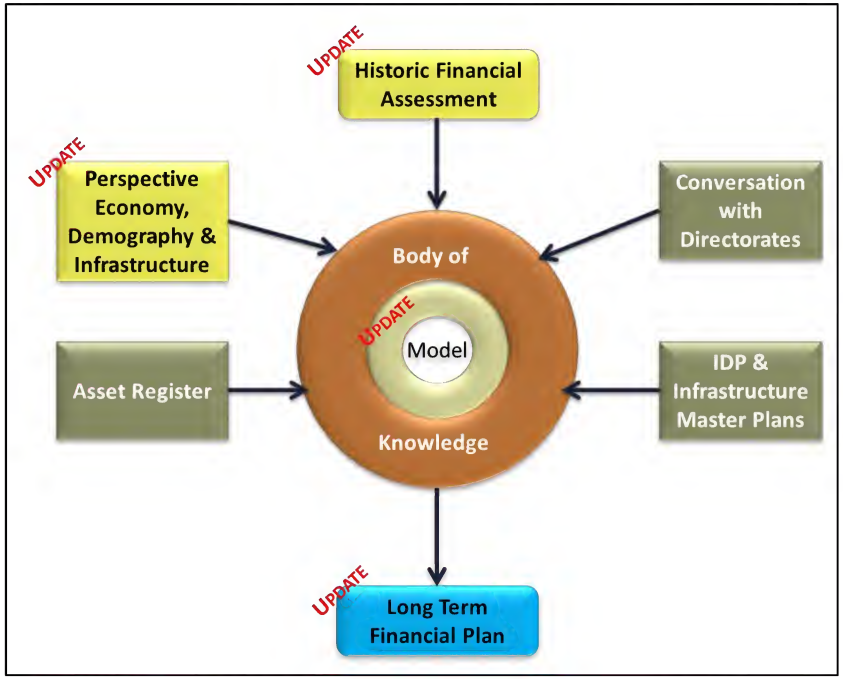
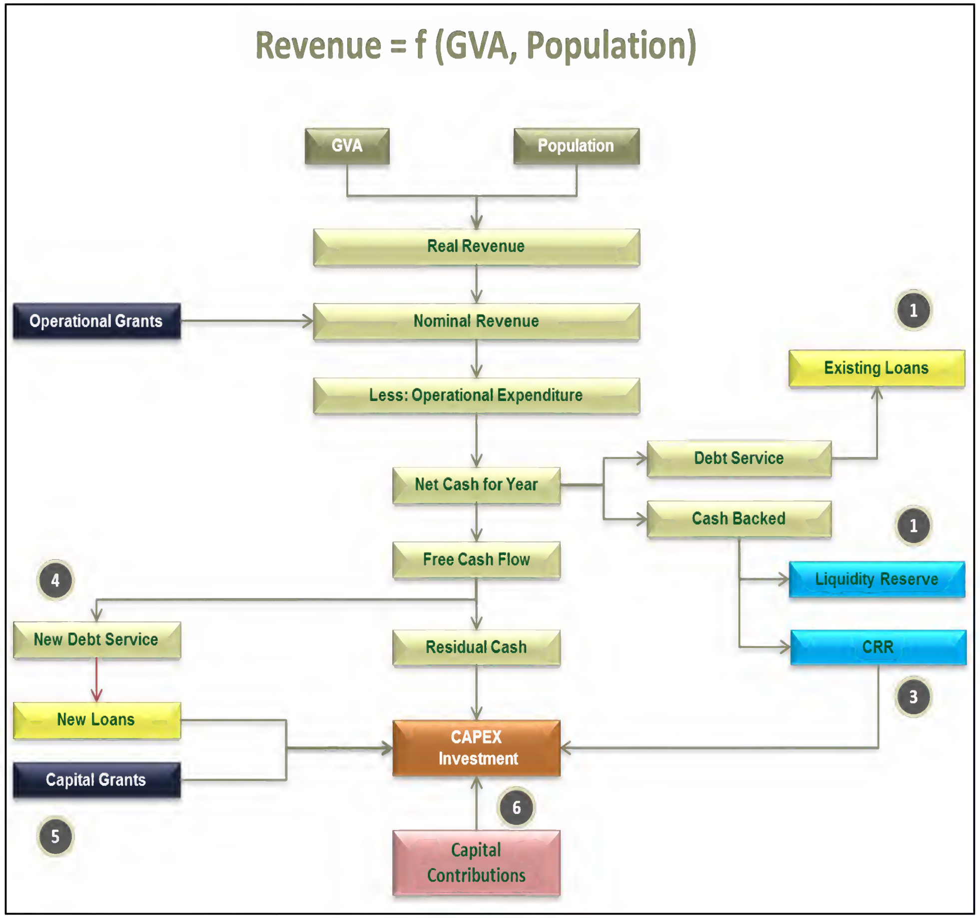
PROCESS

The diagram below illustrates the process followed in preparing a long term financial plan:

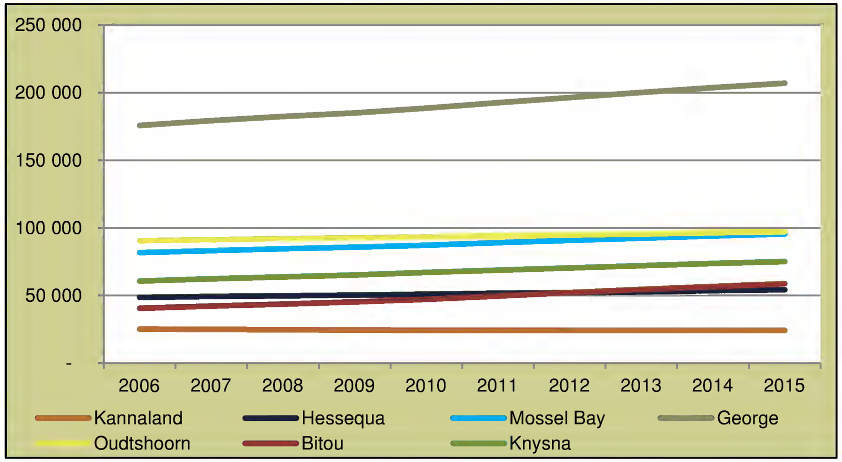


This diagram illustrates the process followed to determine the affordable future capital expenditure based on the revenues that the municipality is expected to generate.

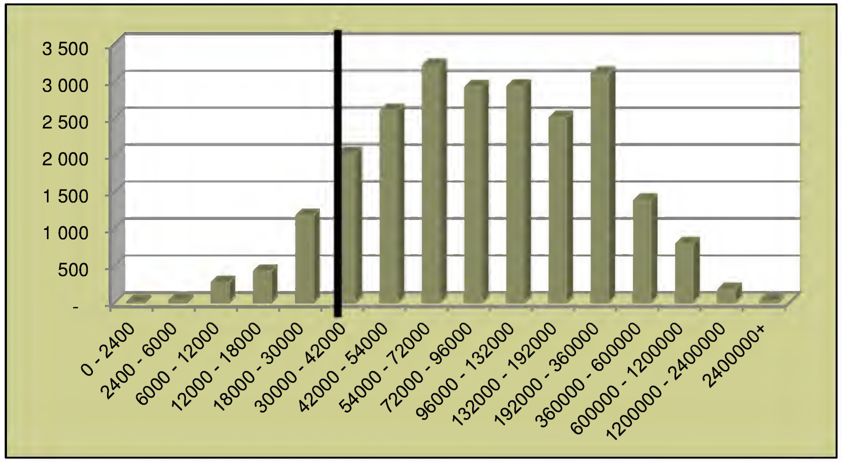


DEMOGRAPHY

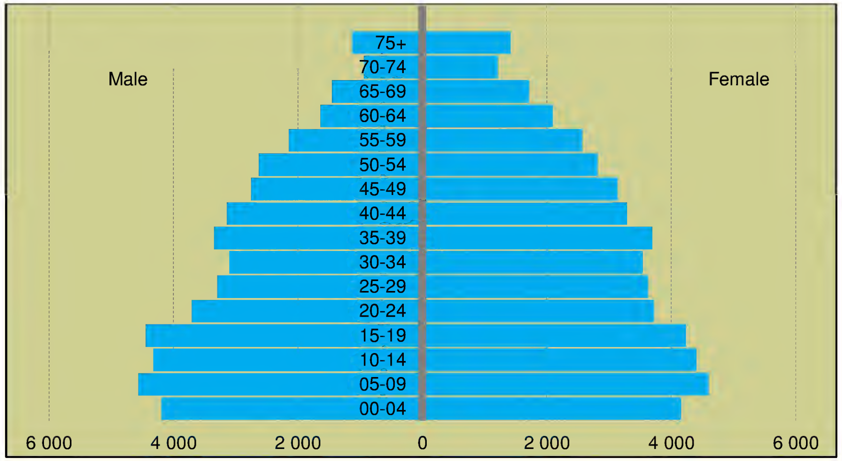
The current estimated ***Population*** of Oudtshoorn is 97 946 (2016). Oudtshoorn currently has the second lowest population growth rate (0.8%) of the seven municipalities in the District and is also lower than the Western Cape (1.6%) and National growth rates (1.5%).



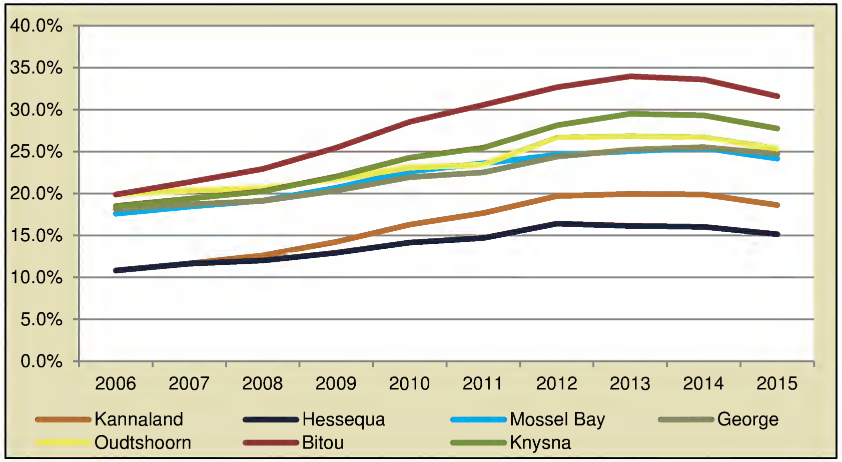
The ***Household Income*** distribution illustrates that the proportion of households earning less than R 30 000 p.a. constitute approx. 8%.



The ***Age Profile*** approximates the classical pyramid with a large base of younger people and fewer older people.

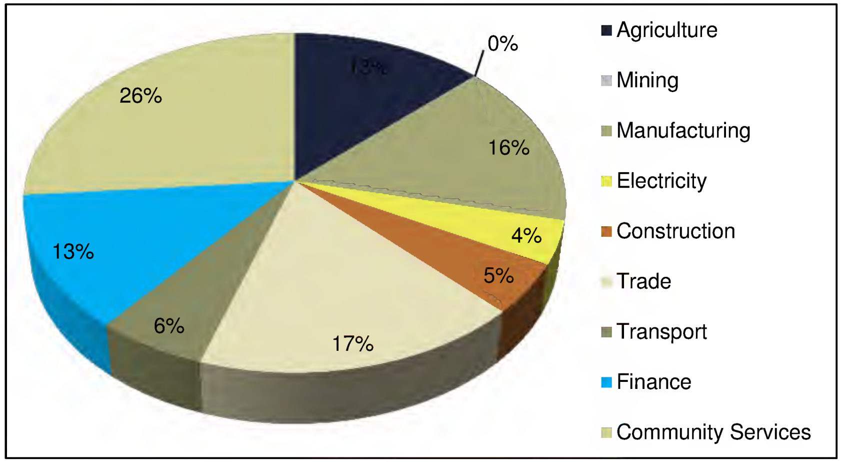


The ***Unemployment Rate*** for 2015 is the third highest of the seven municipalities in the District at 25.3%, and higher than the Western Cape unemployment rate of 21.7% and on par with the National official rate of 25.5%.

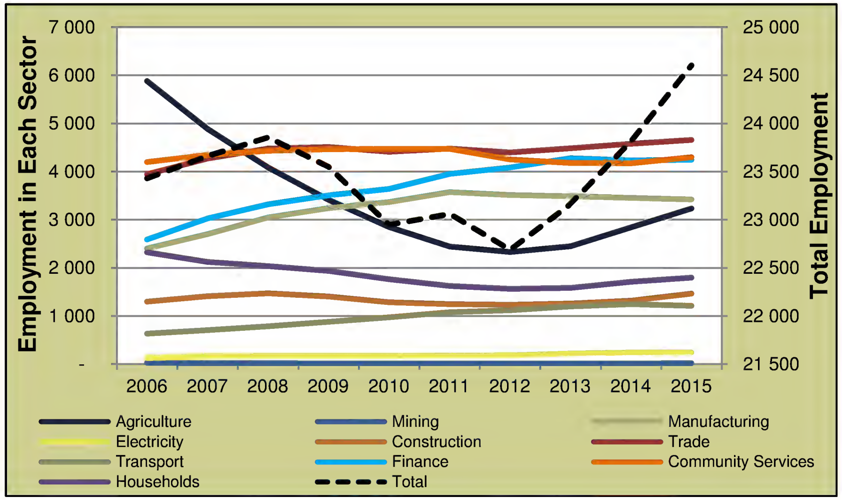


ECONOMY

Community Services remains the dominant ***Economic Sector*** with 26.3% of the output in 2015, followed by Trade (17.4%) and Manufacturing (15.6%).



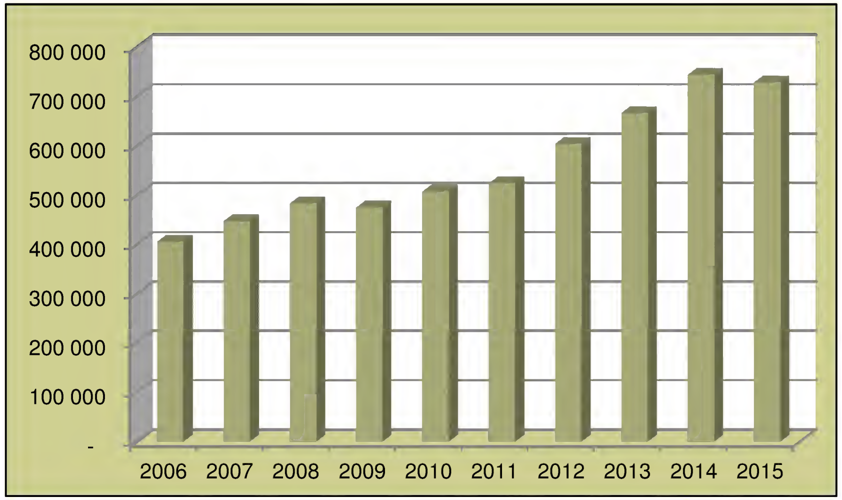
The Trade sector is the largest Employer with 18.9% of total employment; with Community services and Finance contributing 17.5% and 17.3% respectively. After Oudtshoorn suffered a substantial decrease in employment from 2008 to 2012, total employment showed a significant improvement since then. At the end of 2015 the officially registered workers came to 24 604 people.



Proportional growth was experienced in the Finance and Agriculture Sectors, with all other sectors experiencing stagnant or a decline in growth from 2006 to 2015. Although Agriculture showed an Increase from 2006 to 2015, it has shown a small but steady decrease since 2014.

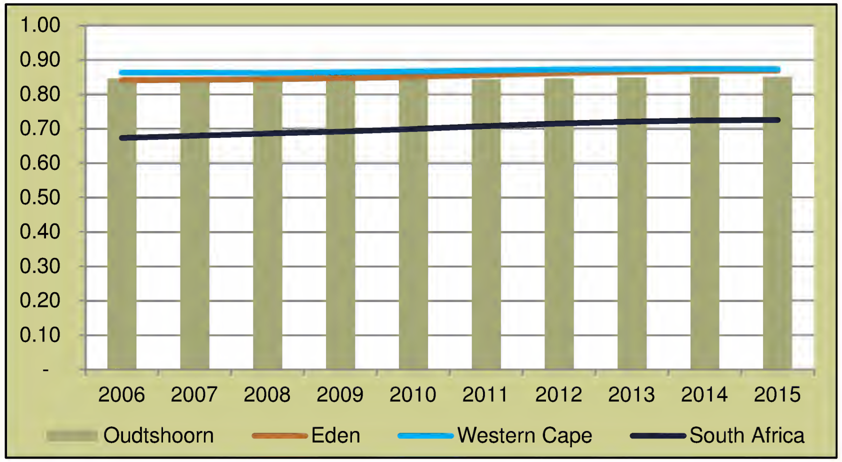
Sector	2006	2015
1 Agriculture	12.2%	13.0%
2 Mining	0.1%	0.1%
3 Manufacturing	17.2%	15.6%
4 Electricity	3.8%	4.1%
5 Construction	4.3%	4.9%
6 Trade	17.9%	17.4%
7 Transport	5.3%	5.8%
8 Finance	11.5%	12.8%
9 Community services	27.7%	26.3%

Tourism Spend amounted to 14.2% of GVA, a slight decrease when compared to 15.2% of 2014. Tourism remains an important economic driver for the local economy.

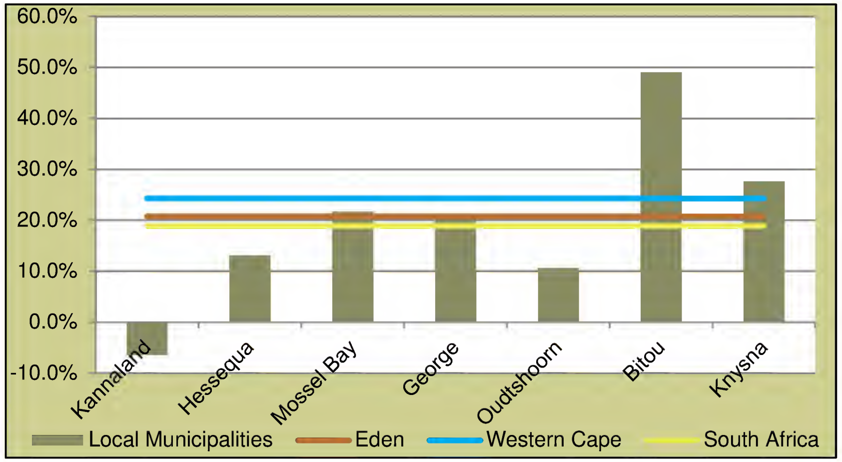


HOUSEHOLD INFRASTRUCTURE

The ***Infrastructure Index*** of 0.85 is lower than the average for the Province and the District and is indicative of infrastructure backlogs. The provision of infrastructure did not keep pace with household formation.



Growth in ***Household Formation*** between 2006 and 2015 was 11%, the second lowest of all seven municipalities in the district. In absolute numbers, the growth of households in Oudtshoorn was 2 268, which was the third lowest during this period.



By comparing backlogs of ***sanitation, water, electricity and refuse removal*** in urban as well as non-urban areas, Oudtshoorn Municipality performed better with regards to water and worse with regards to sanitation, electricity and refuse removal than the average of all the municipalities in the Eden District.

Infrastructure	Eden DM	%	Oudtshoorn	%
Above RDP Level				
Sanitation	127 304	86.1%	18 098	85.0%
Water	140 256	94.8%	20 443	96.0%
Electricity	133 163	90.0%	18 904	88.8%
Refuse Removal	131 132	88.7%	17 209	80.8%
Below RDP Level or None				
Sanitation	20 596	13.9%	3 194	15.0%
Water	7 644	5.2%	848	4.0%
Electricity	14 737	10.0%	2 388	11.2%
Refuse Removal	16 769	11.3%	4 083	19.2%
Total No. of Households	147 900	100.0%	21 292	100.0%

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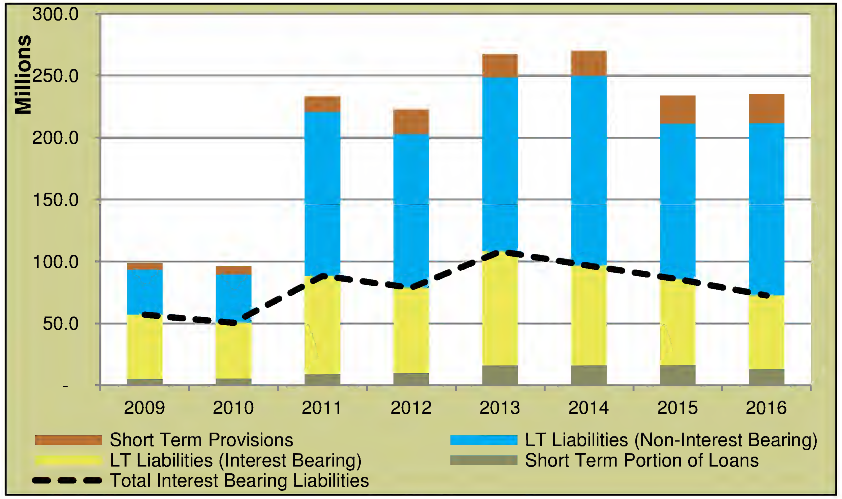
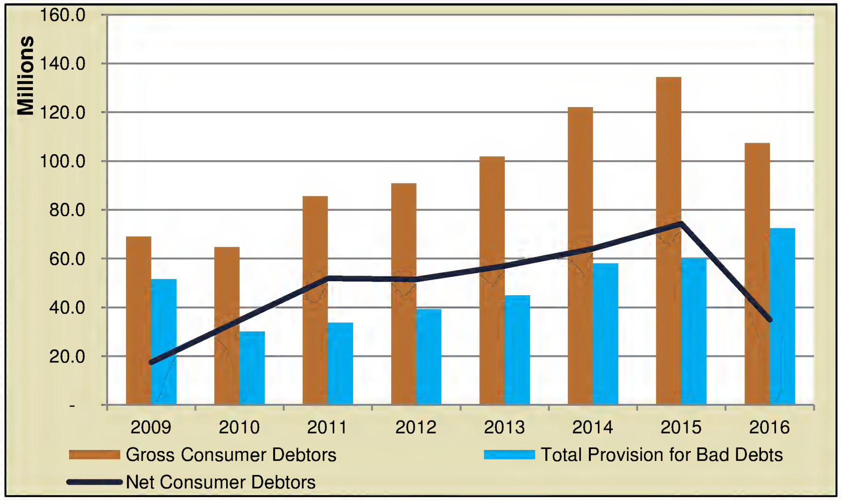
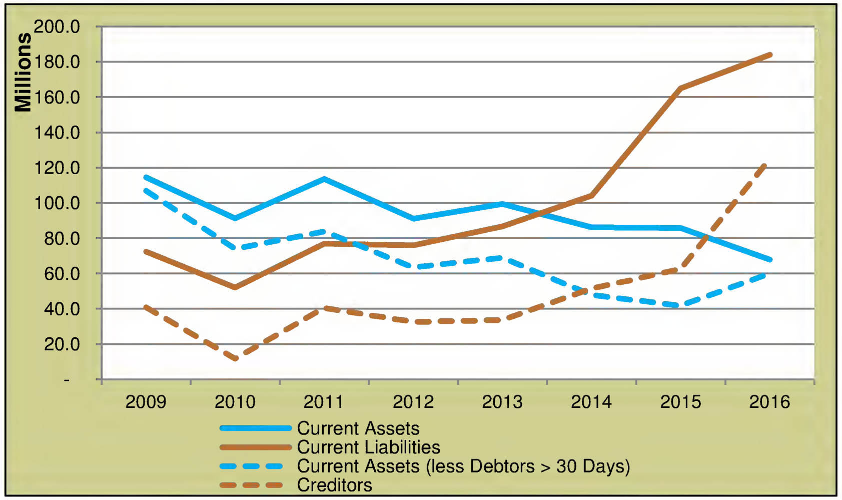
Financial Position

Total Interest Bearing Liabilities continued its decreasing trend since FYE2013 and amounted to R 72.67 m as at FYE2016. The decline was mainly due to the repayment of ***Long Term Interest Bearing liabilities*** (14%). Total ***Non-Interest Bearing Liabilities (Employee benefits and provisions)*** increased by R 14.10 m (10%) and amounted to R 162.20 m at FYE2016. The movement was mostly influenced by a 14% growth in ***Employee Benefits***.





Debtors Collection Rate shows a consistent improvement from 93% in 2014 to 96% in 2015 and 98% in 2016. Provision for bad debts cover 95% of outstanding debtors of 90 days and older compared to 66% the previous year. A total of R 34.58 m in uncollectable debtors was written off during 2016. The combination of the above, results in a 20% or R 27.02 m decrease in Gross Consumer Debtors, and a 53% or R 39.39 m decrease in Net Consumer Debtors.

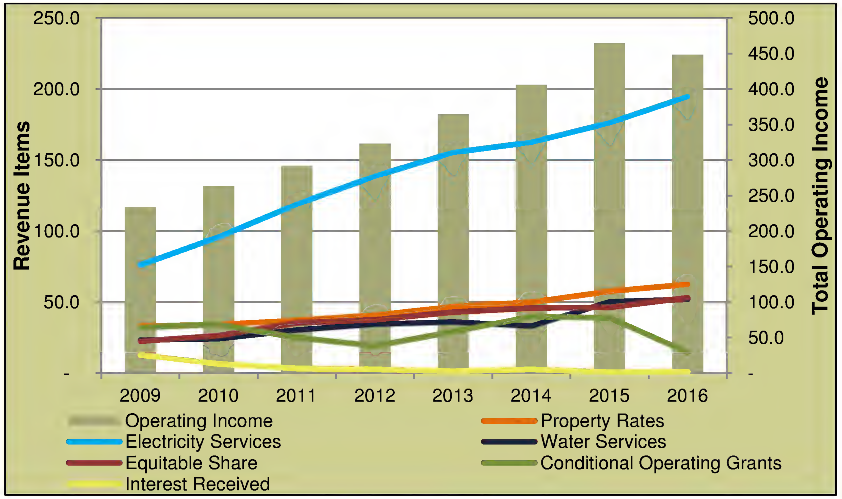


Current Assets at FYE 2016 decreased by R 17.95 m to R 67.82 m and did not cover Current Liabilities, which grew by R 19.72 m to R 184 m. Creditors increased significantly with (111%) or R 62.37 m to R 119.89 m at FYE 2016. (Creditors constituted 68% of Current Liabilities).

The normal liquidity ratio (Current Assets: Current Liabilities) reflect a further weakening from 0.52 in 2015 to 0.37 in 2016. However the Quick Liquidity Ratio (Current Assets less debtors > 30 days: Current Liabilities) improved from 0.25 in 2015 to 0.33 at FYE2016. This is mainly due to the bad debt write-off amounting to R34.58 m and improvement in the collection rate by 2% to 98%.

Although the liquidity ratio has weakened, it has had the effect that the quality of the assets improved. The increase in creditors was due to a discovery of unaccounted for payables in the past. The municipality has entered into payment arrangements with is creditors.

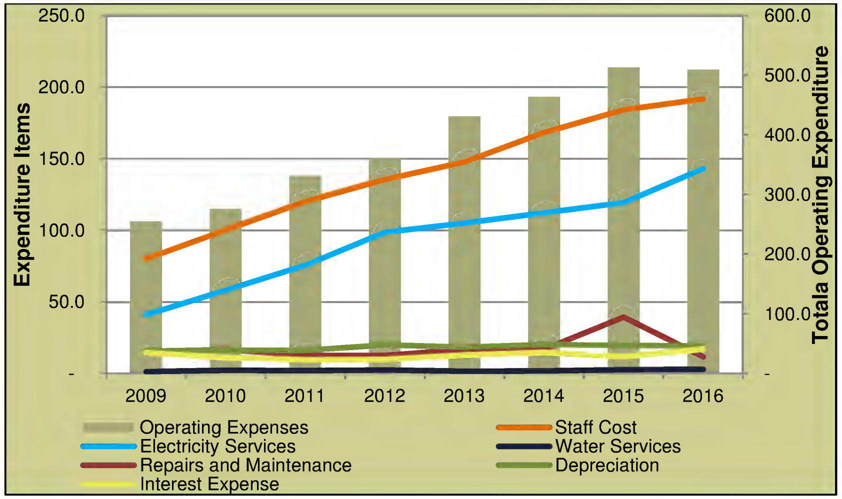
INCOME AND EXPENDITURE



Total Operating Income (excluding Capital Grants) decreased slightly by R 18.67 m (4%) to R 448.30 m in FY2016, from the prior year.

The main revenue generating items remained the same proportionally, dominated by sales of ***Electricity Services*** contributing 43%, ***Property Rates*** (14%), ***Equitable Share*** (12%) and ***Water Services*** (12%).

Conditional Operating Grants reflect a 64% decrease (R24.32 m) to R 14.68 m and constituted 3% of ***Total Operating Income*** as at 30 June 2016.



Total Operating Expenditure decreased slightly by R 3.24 m (1%) to R 510.00 m in FY2016. Of particular concern is that the Municipal Expenditure continued to exceed its Operating income (excluding capital grants) in the past 8 financial years.

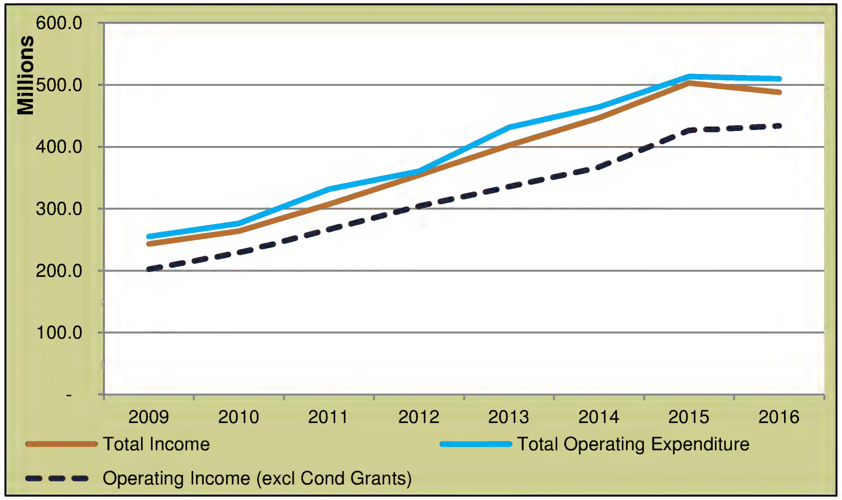
Salaries, Wages and Allowances remained a dominant expenditure item, increasing by R 7.44 m (4%) to R 191.74 m in FY2016. The Staff costs/total expenditure ratio of 35% is within the municipal norm of 25%-40% set by National Treasury.

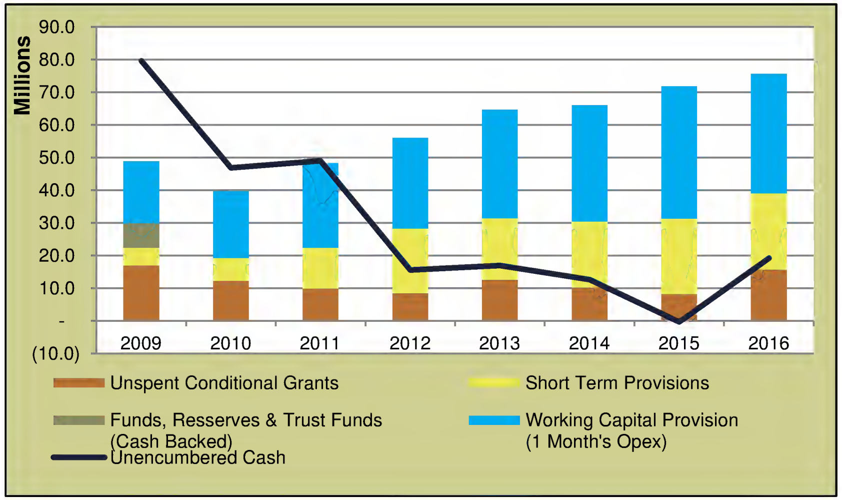
Expense associated with ***Electricity Services*** increased by R 23.64 m (20%) and constituted 26% of ***Total Expenditure*** in FY2016.

Debt Impairment increased significantly (77%) to R 50.95 m in FY2016. This movement was largely attributed to a major increase in the provision for ***Trade Receivable from Exchange Transactions,*** which amounted to R 40.23 m during the same period.

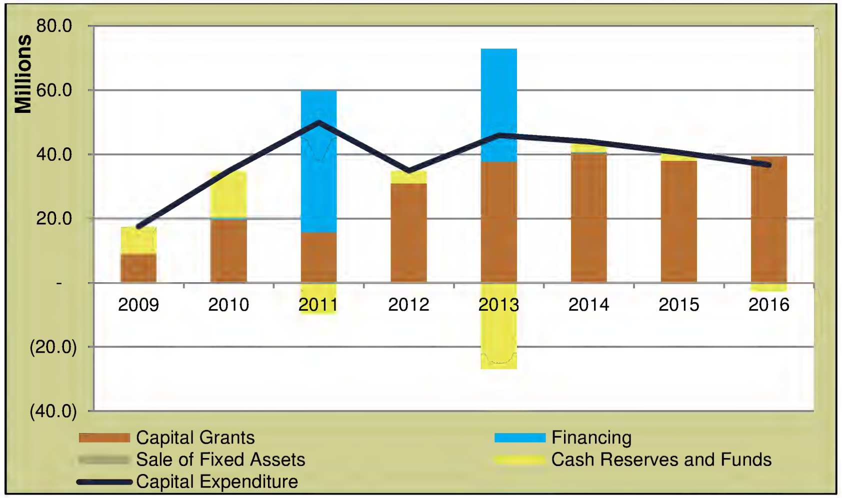
Cash Flow

Total Operating Expenditure continued to exceed ***Total Operating Income*** during the 8 year assessment period**.** Since FY2013, Capital Expenditure decreased and amounted to R 36.71 m in FY2016. Furthermore, Operating Income decreased slightly from a high of R 465.42 m in FY2015 to R 448.63 m during the year under review.





Proportionally ***Capex*** reflects a decreasing trend since FYE2013 and amounted to R 36.71 m at FYE2016 (FYE2015 – R 40.59 m) which was only funded by ***Government Grant Funding*** at R 39.37 m.



The municipality was not once during the last 5 financial years been able to hold cash resources, equivalent to the minimum required liquidity[1]. Cash at FYE2016 amounted to R 19.16 m, which was R 56.5 m less than the minimum liquidity required.

Unspent Conditional Grants increased by R 7.44 m to R15.6 m, while Short Term Provisions remained fairly constant and currently stands at R 23.39 m.

[1] For purposes of this report the minimum required liquidity as applied by IPM consists of short term provisions, unspent conditional grants, reserves and 1 month working capital.

MINIMUM LIQUIDITY LEVEL

MINIMUM LIQUIDITY LEVELS	2009	2010	2011	2012	2013	2014	2015	2016
Unspent conditional grants	16.9	12.2	9.9	8.4	12.5	10.2	8.2	15.6
Short term provision	5.4	7.0	12.4	19.8	18.8	20.2	23.1	23.4
Funds, Reserves & trust funds (Cash Backed)	7.5	-	-	-	-	-	-	-
Total	**29.8**	**19.2**	**22.3**	**28.2**	**31.3**	**30.4**	**31.2**	**39.0**
Unencumbered Cash & Cash Equivalents[2]	79.6	46.9	49.0	15.6	17.0	12.6	(0.3)	19.2
Cash Coverage Ratio (excluding Working Capital)[3]	**2.7**	**2.4**	**2.2**	**0.6**	**0.5**	**0.4**	**(0.0)**	**0.5**
Working Capital Provision [1 month Opex][4]	19.1	20.5	26.0	27.9	33.3	35.7	40.6	36.6
Cash Coverage Ratio (including Working Capital)[5]	**1.6**	**1.2**	**1.0**	**0.3**	**0.3**	**0.2**	**(0.0)**	**0.3**
Minimum Liquidity Required[6]	48.9	39.7	48.3	56.1	64.7	66.0	71.9	75.7
Cash Surplus/(Shortfall)[7]	**30.7**	**7.2**	**0.7**	**(40.5)**	**(47.7)**	**(53.4)**	**(72.2)**	**(56.5)**

[2] Unencumbered cash and cash equivalents = Total cash and cash equivalents-Ceded investments
[3] Cash Coverage Ratio (excl. Working Capital) = Unencumbered cash and cash equivalents/Total
[4] Total Expenditure less Non-Cash Items/12
[5] Unencumbered cash and cash equivalents/(Total + Working Capital provision)
[6] Total + Working Capital Provision
[7] Minimum liquidity required - Unencumbered cash and cash equivalents

HISTORIC FINANCIAL RATIOS

Ratio	2009	2010	2011	2012	2013	2014	2015	2016
Liquidity Ratio (Current Assets : Current Liabilities)	1.58	1.76	1.47	1.20	1.15	0.83	0.52	0.37
Quick Liquidity Ratio (Current Assets less Debtors > 30 Days : Current Liabilities)	1.48	1.42	1.09	0.84	0.79	0.46	0.25	0.33
Payment Ratio / Collection Rate		89%	90%	98%	93%	93%	96%	98%
Gearing: Total Debt (Borrowings) / Operating Revenue	24%	19%	30%	24%	30%	24%	18%	16%
% Increase in Billed Income p.a.		14%	22%	13%	17%	-1%	12%	8%
Total Grants / Total Revenue	26%	23%	25%	25%	27%	28%	25%	22%
Own Source Revenue to Total Operating Revenue	77%	77%	79%	82%	80%	79%	82%	85%
Staff Costs / Total Operating Expenditure	29%	32%	32%	34%	31%	33%	33%	35%
Repairs and Maintenance as % of PPE and Investment Property	9%	8%	2%	2%	3%	2%	5%	2%
Capital Expenditure / Total Expenditure	6%	11%	13%	9%	10%	9%	7%	7%
Net Operating Surplus / Total Operating Revenue	-9%	-5%	-14%	-11%	-18%	-14%	-10%	-14%
Electricity Surplus / Total Electricity Revenue	46%	39%	37%	29%	32%	31%	32%	27%
Water Surplus / Total Water Revenue	94%	91%	93%	92%	96%	95%	95%	94%
Debt Service Cover Ratio (Cash Generated by Operations / Debt Service)	-0.19	-1.23	0.57	-1.05	-1.07	-0.60	-2.26	2.55
Cash Generated by Operations / Total Operating Revenue	-3%	-9%	3%	-6%	-6%	-4%	-11%	17%
Cash Coverage Ratio (excl Working Capital)	2.67	2.45	2.19	0.55	0.54	0.42	-0.01	0.49
Cash Coverage Ratio (incl Working Capital)	1.63	1.18	1.01	0.28	0.26	0.19	-0.00	0.25
Cash Surplus / Shortfall on Minimum Liquidity Requirements	30.70	7.18	0.67	-40.54	-47.69	-53.44	-72.20	-56.51

OUTCOME OF THE INDEPENDENT FINANCIAL ASSESSMENT

The Department of Co-Operative Governance and Traditional Affairs (COGTA) intervened in the municipality in terms of section 139(1)(b) of the Constitution in August 2015, as a corrective measure of last resort. In July 2016 a Financial Recovery Plan was published for comments as required by legislation in terms of section 139 of the Constitution read together with section 142 of the MFMA. The comments below should be read, keeping this perspective in mind.

Oudtshoorn received an adverse audit opinion for FYE 2015 but it seems as if a qualified Audit opinion can be expected for FYE2016. Oudtshoorn posted a Cash Operating Surplus (Excluding capital grants) as at FYE2016. The surplus grew significantly to R 77.00 m during the FY2016 compared to a deficit of R 51.70 m posted in the previous financial year.

The Municipality's liquidity ratio continued its declining trend, and became the worst over the eight year period and currently stands at 0.38:1. The unhealthy liquidity ratio is mainly attributed to a 111% increase in ***Creditors***, 165% increase ***in Unspent Conditional Grants*** and 45% decrease in ***Consumer and Other Debtors***'. Creditors and Unspent Conditional Grants constituted 68% and 8% of Current Liabilities respectively, while Consumer and Other Debtors constituted 71% of Current Assets. This was largely due to a cleaning up of the books, viz. improving the quality of the current assets by writing off uncollectable bad debt and accounting for creditors, that were previously not recorded and entering into payment arrangements with these creditors.

Payables from exchange transactions increased significantly by R 63.1 m (111%) and amounted to R 119.89 m during FY2016.

The municipality reported a collection rate of 98%. The collection level increased by 2 percentage points compared to the previous year. This level is above the municipal norm of 95% set by National Treasury.

Salaries and Wages increased by 4% to R 191.74 m in FYE2016 and constitute 35% of Total Expenditure compared to 33% in the previous year. The Staff costs/total expenditure ratio of 35% is within the municipal norm of 25% - 40% set by National Treasury.

Gross Consumer Debtors continued an increasing trend since FYE2011 and averaged a growth of 12% annually in the last five years (2011-2015). Provision for Bad Debts has also increased during the same period to R 60.81 million and almost covers debtors older than 90 days (95%) in FYE2016. The highest proportion of debtors' is held in water services (27%), electricity services (20%) and sewerage rates (19%). Debtors older than 90 days continued to be dominant and constituted 71% of Consumer Debtors in FYE2016. Bad debts written off on rates and service debtors amounted to R 34.58 million in FYE2016 (R 0 – FYE2015). In 2016 Gross Consumer debtors declined by R27.0 million to R107.5 million, mainly as a result of bad debts of R34.58 million written-off.

Over the past eight assessed years, Total Operating Income (Excluding Capital grants) was lower than Total Expenditure. It follows that Accounting Deficits were experienced in all of the eight years. This evidences an unhealthy financial state of affairs..

The External Gearing has decreased in the past four financial years and is currently at 16%. Gearing remained below the recommended norm of 40% however (National Treasury recommends a maximum of 45%).

Unencumbered Available Cash remains low - a trend that started in FY2012. Cash and cash equivalents amounted to R 19.76 m at FYE2016, which is below the minimum required liquidity to cover all statutory requirements, including one month's working capital of R 75.70 m. This represents a positive turnaround from a cash shortfall position of R48.02 million in the previous financial year.

Capital expenditure decreased by R 3.90 m (10%) and amounted to R 36.70 in FYE2016 (FYE2015 – R 40.60 m). The funding mix consists of Capital

Grants of R 39.4 m (107%), which was the main funding source, and Cash Reserves and Funds of -R 2.80 m (-7%) during the same period.

Net Cash from Operating Activities increased by R 130.43 million (112%) in FYE2016 from -R 13.88 million in the previous year. Net Cash flow from Investing Activities decreased by R 4.79 million (15%) from R 31.80 million in FYE2015. The municipality improved its cash position, mainly due to a decrease of R141.48 million in Payments to Suppliers and employees, in the amount of R 343.55 million in FYE2016, from R 485.03 million in the previous year.

The net result is that although a Net deficit in the Statement of Financial Performance of R22.13 million was experienced at FYE2016, the net movement in cash was a positive R67.28 million in FY2016, versus a negative movement of R60.34 million in 2015, largely due to a decrease in payments to suppliers and employees.

Key Strengths

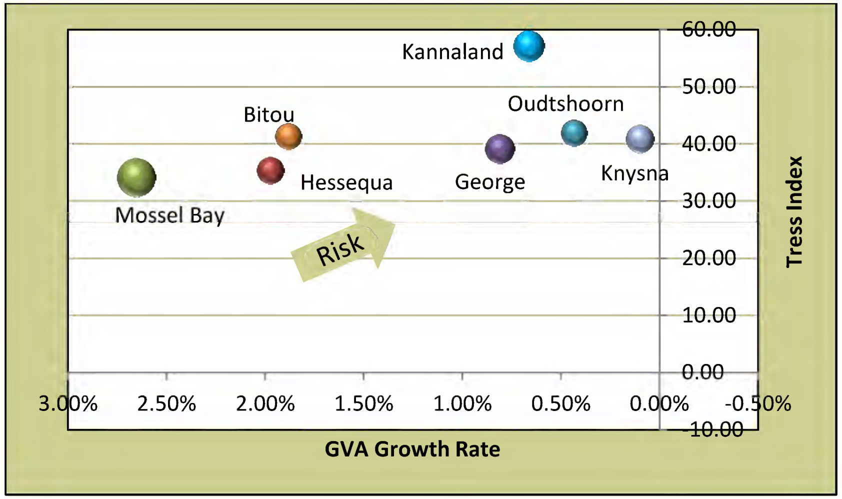
- Positive cash balance at FYE2016 of R19.76 m versus a negative balance of R 47.52 m the previous year;
- Collection rate of 98%;
- Relative low gearing at 16%;
- Clear arrangements with creditors as to payments due.

Key Weaknesses

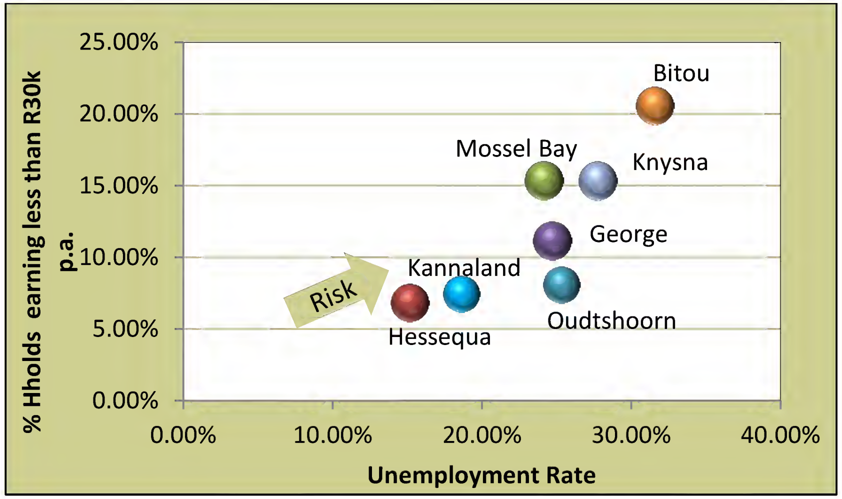
- Liquidity ratio at 0.37 :1 at FYE 2016 mainly due to a substantial increase in payables;
- Continuation of Accounting deficits experienced over the eight year period in FY2016;
- Cash shortfall of R 56.5 m below the IPM recommended minimum required liquidity at the end of FY2016;
- Low level of unencumbered cash at FYE2016;
- Reliance on Government grants for capital expenditure;
- Substantial decrease in cash payments to suppliers and employees, which in the light of the precarious financial position of Oudtshoorn may be seen as a positive;
- Inconsistent trends disclosed in both income and expenditure sources.

MUNICIPAL REVENUE RISK INDICATOR (MRRI)

Oudtshoorn has a R 3.5 billion economy (constant 2010 monetary terms). The GVA per Capita of R35 585 is the second lowest in the district. Its average economic growth rate during the past 5 years of 0.4% p.a. was disappointing, with only Knysna performing worse. The economy in Oudtshoorn is less diversified than the majority of the other municipalities as evidenced by the Tress Index. The combination of these factors resulted in an ***Economic Risk*** component of the MRRI for Oudtshoorn of *Very High*.



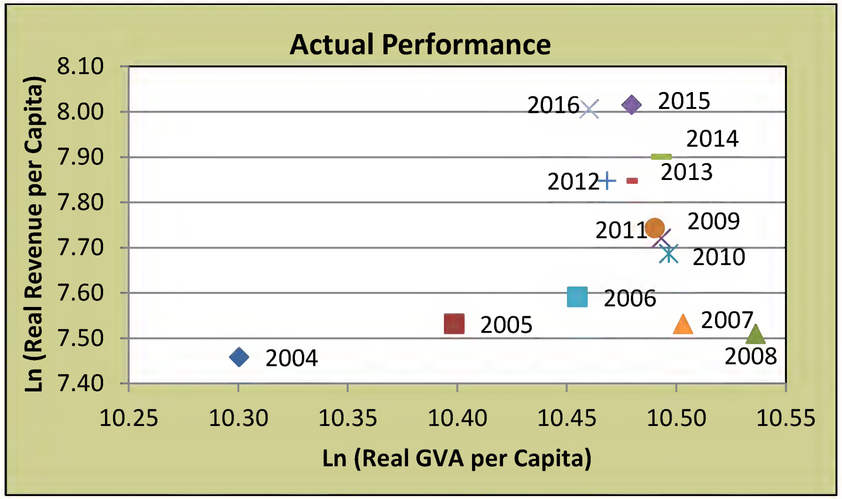
The unemployment rate of 25.3% is on par with that of Mossel Bay and George. The percentage of households earning less than R30 000 p.a. of 8.1% is relatively low, but the Human Development Index of 0.65 is together with Kannaland the lowest in the district. These factors combine to provide a *Medium to High* ***Household Ability to Pay Risk*** component of the MRRI.



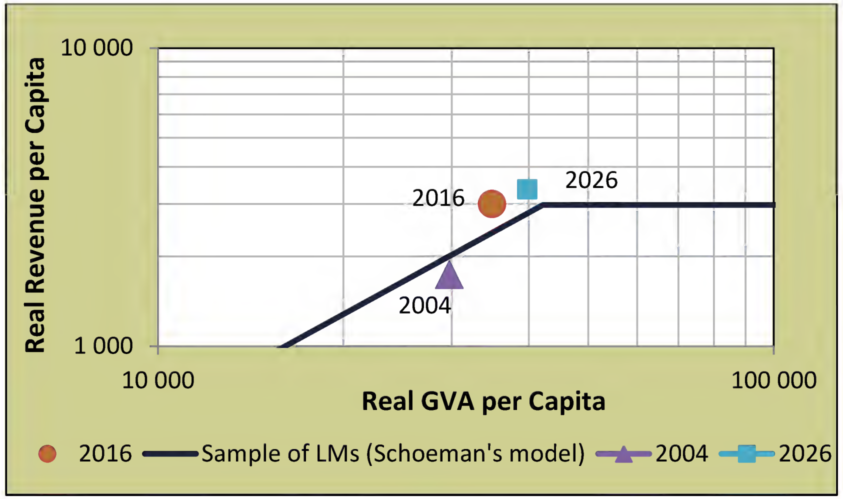
The resultant ***Municipal Revenue Risk Indicator ("MRRI")***, which is a weighted average of the Economic Risk and Household Ability to Pay Risk is ***High***. There is a high risk that the municipality will not be able to generate sufficient own revenue and is highly dependent on Government Transfers.

THE REAL MUNICIPAL REVENUE PER CAPITA AND REAL GVA PER CAPITA RELATIONSHIP

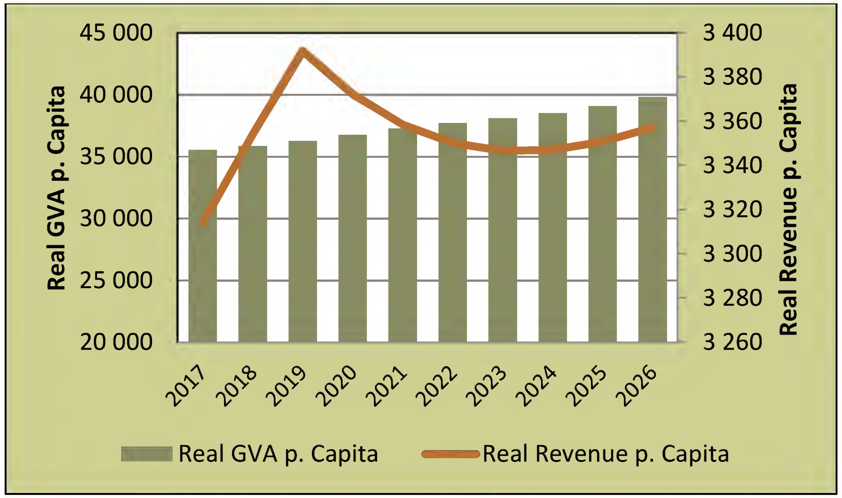
The relationship between the ***Real GVA per Capita*** and ***Real Municipal Revenue per Capita*** between 2004 and 2016 showed an inconsistent trend. Generally before 2007 Municipal Revenue per Capita increased with an increase in GVA per Capita. However, since 2008, the trend was counterintuitive in that the Real Municipal Revenue per Capita increased albeit against a decline in Real GVA per Capita.



In 2004 the ***Real Revenue per Capita*** for Oudtshoorn was below the expected amount for the Real GVA per Capita as researched by Schoeman[8]. In 2016 the ***Real Revenue per Capita*** exceeded the expected amount slightly. In real terms the projected revenue per capita in 2026 is even more than the revenue per capita in 2016 and exceeds the amount predicted in Schoeman's model. This requires a concerted effort by the municipality to promote local economic development and protect and enhance its revenues, without which it will not be able to achieve the ambitious revenue estimates.



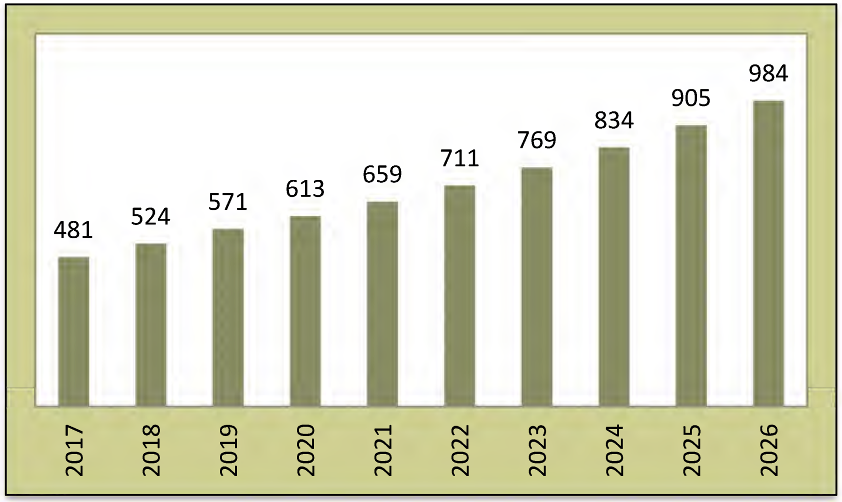
Largely due to the projected economic growth rate exceeding the population growth rate, the Real ***GVA per Capita*** shows a slight increase during the 10-year period. The revenue growth per capita as envisaged in ODM's MTREF up to 2018/19 is not expected to last for the 10-year planning period and ***Real Revenue per Capita*** is expected to decline marginally from a high of R 3 390 p.a. to approximately R 3 350 p.a. before increasing again slightly.



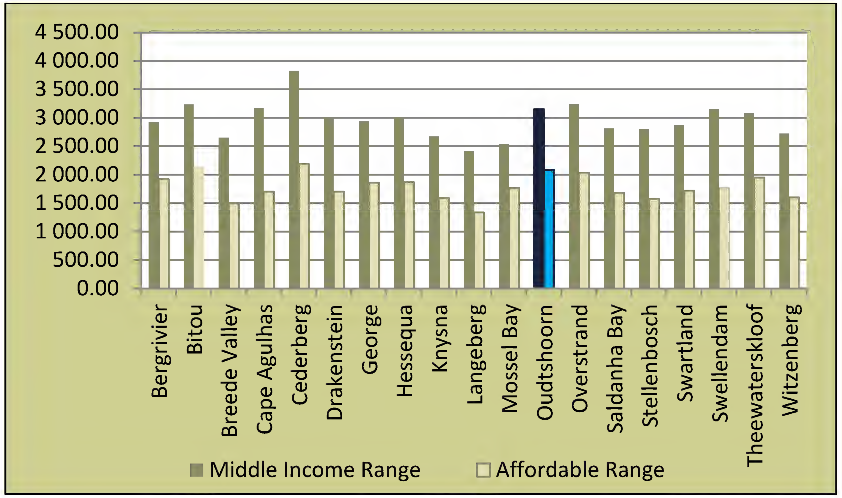
[8] *Fiscal Performance of Local Government in South Africa - an Empirical Analysis*; Niek Schoeman; UP 22 July 2011; https://editorialexpress.com/cgi-bin/conference/download.cgi?db_name=IIPF67&paper_id=40

FUTURE NOMINAL REVENUES

Based on the assumptions made in the Financial Model (see further on in this report), the ***Future Nominal Municipal Revenue*** (excluding Grants) is growing at an average rate of 10.5% p.a. This is a combination of (i) tariff increases (ii) increased sales and (iii) additional revenue sources.



A comparison of the ***Average Household Bill*** for the Middle Income- and Affordable Ranges of a selected number of municipalities in the WC, based on the 2016/17 tariffs reveals that Oudtshoorn features in the 2nd Quartile for the Middle Income Range and in the top Quartile for the Affordable Range. Very little scope exists to increase rates and tariffs proportionally more than the average increases.



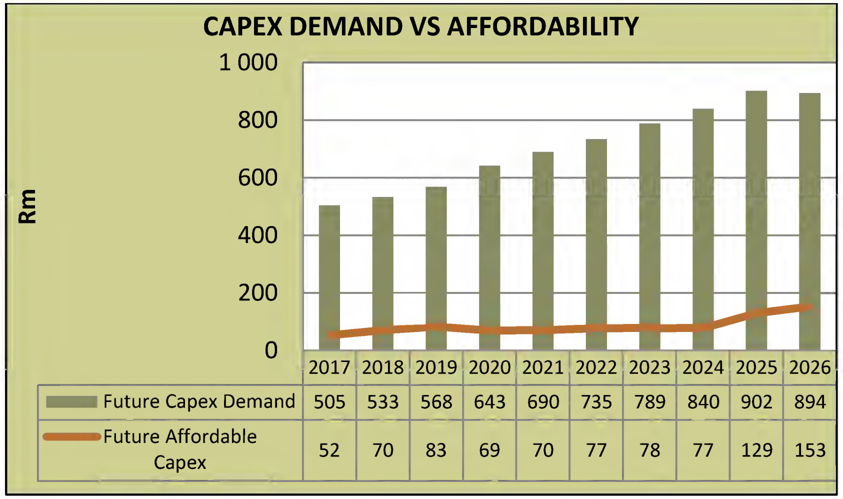
1	Planning Process
2	Updated Perspectives (Demographic, Economic, Household Infrastructure)
3	Updated Historic Financial Assessment
4	Future Revenues
5	**Affordable Future Capital Investment**
6	Scenario Analysis
7	Ratio Analysis
8	Conclusions

Capex Affordability and Funding

Capex Affordability vs Demand

Total 10-year Capex **Demand**	=	R 7 099 million
Total 10-year Capex **Affordability**	=	R 859 million

The Capex Demand exceeds the Capex Affordability as illustrated in the Graph below. It needs to be stressed however that the capex demand estimates were based on the work done in 2016, which included an analysis of the Asset Registers and IPM's estimates of new capital investments and need to be revised pursuant to updated Master Plans.



Oudtshoorn's MTREF budget 2016/17 to 2018/19 expects a capital funding mix that amounts to R 180.5 million and consists of the following:

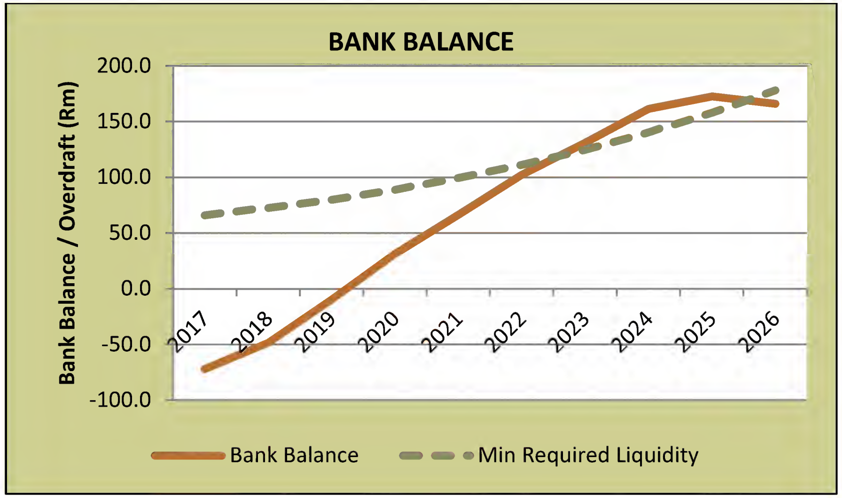
R'000 000	*Total*	*2017*	*2018*	*2019*
Loans	0.0	0.0	0.0	0.0
Cash	10.1	4.8	3.0	2.3
Grants	170.4	42.5	57.0	70.8
Total	**180.5**	**47.4**	**60.0**	**73.2**

The municipality's current liquidity position is unhealthy and increasing external financing and internally generated funding would be irresponsible. The MTREF Capital budget is deemed to be prudent.

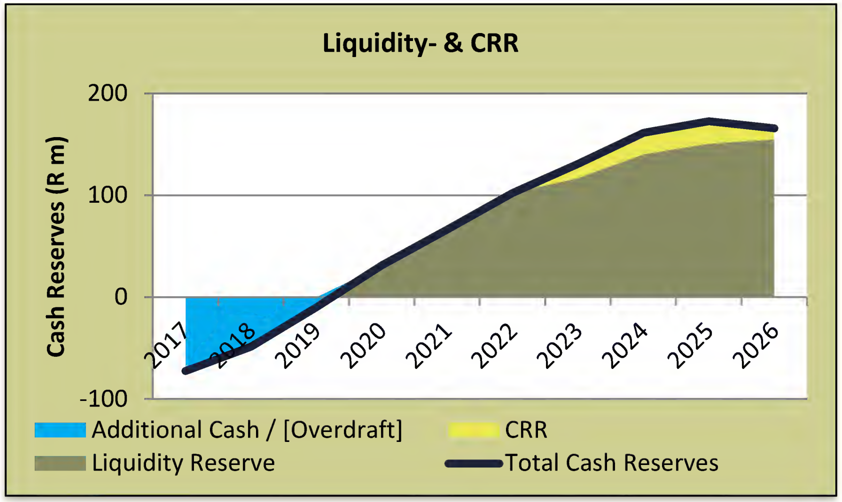
Liquidity

For purposes of this report the minimum required liquidity level caters for unspent conditional grants, reserves, short term provisions, and 1 month working capital.

The cash resources available up to 2022/23 are less than the minimum liquidity required, as illustrated below. In fact during the first 2 years the cash book balance is expected to be negative, largely as a result of the change in working capital.



IPM's models were recalibrated based on the latest MTREF budget. On condition that disciplined financial management is maintained into the future, the liquidity position will be reversed. By FYE2020 the municipality will be cash positive and by FYE2023 the cash should exceed the minimum liquidity required.



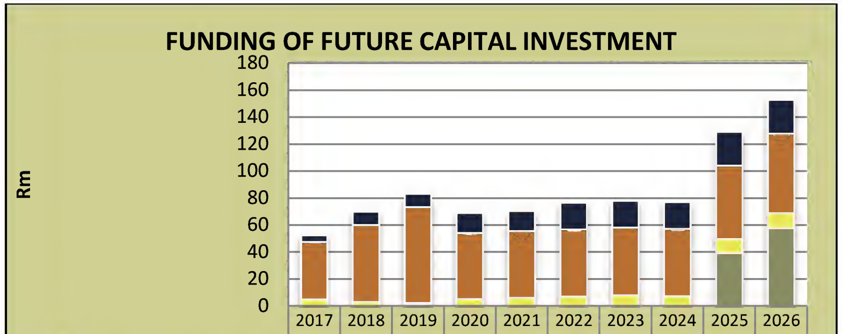
Capital Funding Mix

The 10-year capital funding mix for the Base Case is presented in the table below:

10-YEAR ESTIMATED FUNDING SOURCES		
Source	**Base Case**	**%**
New Loans	R 97	11.3%
Own Cash	R 65	7.6%
Grants	R 532	62.0%
Other	R 165	19.2%
Total	**R 859**	**100.0%**

As indicated in the initial report of July 2016, the anticipated development projects should generate developer's capital contributions. An estimate of these contributions was included under "Other" sources. In the Base Case 62% of capex funding is sourced from Grants. The availability of grants to serve a growing indigent population needs to be assessed in the face of the prevailing national fiscal constraint.

The distribution of the funding mix for the Base Case is presented below:



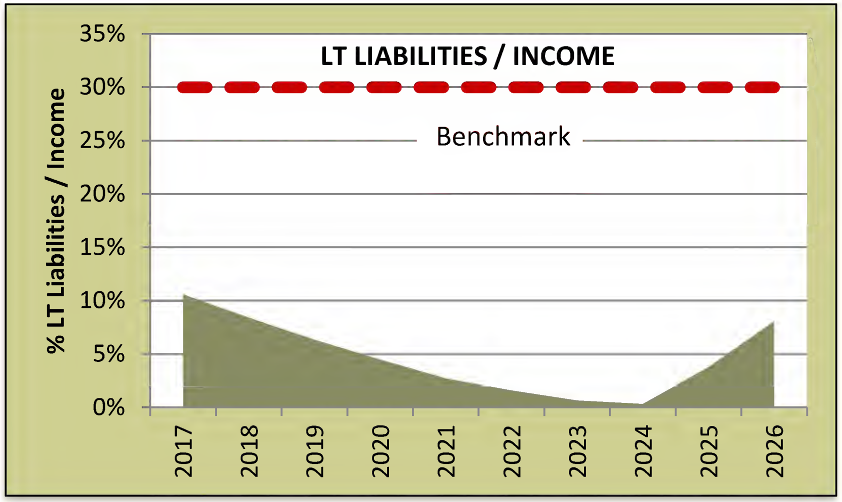
	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026
Other Capital Contributions	5	10	10	15	15	20	20	20	25	25
Grants	43	57	71	49	49	50	50	50	54	59
Own Cash	5	3	2	5	6	7	8	7	11	11
New Loans	0	0	0	0	0	0	0	0	39	58
Existing Loans	0	0	0	0	0	0	0	0	0	0

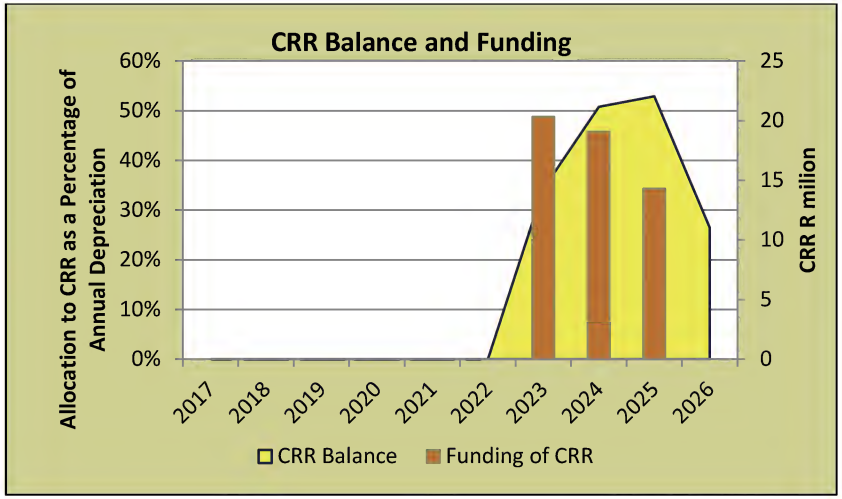
As budgeted in its MTREF up to 2018/19, no new loan funding will be accessed. The priority for the municipality is to build up its liquidity which implies that external financing will only be able to be accessed again in 2024/25.

Gearing

The continuous redemption of existing loans and suspension of new loans results in a declining level of gearing until 2024 after which the take up of new loans results in an increase in gearing, but the level will never exceed the benchmark of 30% proposed for Oudtshoorn. If the negative cash book balance or "overdraft" were to be added to the interest bearing liabilities, the gearing would increase to 24% in 2016/17.

The External Loan Liability Paid Coverage Ratio which should at least be 1:1 and preferably 2:1 never falls below 5:1. See Ratio Table on page 26.





Capital replacement Reserve ("CRR")

Oudtshoorn did not have a CRR as at FYE2016. We proceed from the premise that in future available cash, above the minimum liquidity requirement, will be reserved in a dedicated CRR each year and that 50% of the balance of this reserve is used to fund capital expenditure.

During the initial years, up to 2023, available cash does not allow for the funding of a cash backed CRR. However, liquidity improves from 2022 onwards to allow a gradual increase in the allocation of cash towards such a fund, albeit that the Municipality will not have the resources to cash back the full amount of the depreciation charge.

1	Planning Process
2	Updated Perspectives (Demographic, Economic, Household Infrastructure)
3	Updated Historic Financial Assessment
4	Future Revenues
5	Affordable Future Capital Investment
6	**Scenario Analysis**
7	Ratio Analysis
8	Conclusions

Scenarios

Realistic Upside and Downside Scenarios were compared to the Base Case Scenario.

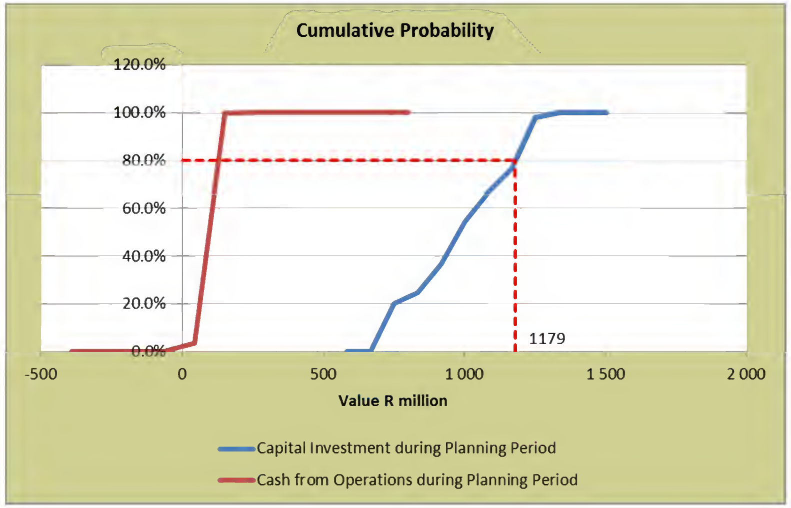
ASSUMPTIONS	BASE CASE	UPSIDE	DOWN-SIDE
Projected GVA Growth Rate p.a.	2.1%	3.8%	1.2%
Projected Population Growth Rate	1.0%	1.0%	1.2%
Year when structural change in salaries & wages is implemented	2020	2020	2020
Structural change in salaries and wages in 2020	0.0%	-5.0%	5.0%
Cost Factor of Salaries & Wages	1.0	1.00	1.05
Cost Factor on Electricity Services	1.0	1.00	1.05
Cost Factor on Water Services	1.0	0.95	1.00
Cost Factor on Repairs & Maintenance	1.0	1.00	1.00
Cost Factor on General Expenses	1.0	0.95	1.00
Collection Rate	93.0%	95.0%	91.0%

OUTCOME	BASE CASE	UPSIDE	DOWN-SIDE
Average annual % increase in Revenue	10.5%	11.3%	10.3%
Surplus accumulated during 10 years	481	1 080	-435
10-year cash from operations after debt service	184	580	-414
10-year LT Debt Raised	97	427	0
10-year capital investment programme	859	1 232	731
Cash investments after 10 years	166	660	-708

For the 10-year period, the Accumulated Surplus remains positive for the Base Case and Upside, but turns negative for the Downside. Cash from Operations ranges between - R 414m and R 580m. The cash position after 10 years is a healthy R 660 m in the Upside but cash negative to the amount of -R 708 m in the Downside. The great variation of outcome for a realistic combination of input variables, demonstrates the need to manage the municipality's finances with care and discipline.

The probability outcome of a Monte Carlo Simulation on the 10-Year Cash after Debt Service and 10-Year Capital Investment Programme is illustrated below. There is a 80% probability that the Capital Programme will be less than app. R 1 179 million and a 3% probability that the cash generated after debt service will be negative.

Cumulative Probability Outcome of Monte Carlo Simulation



1	Planning Process
2	Updated Perspectives (Demographic, Economic, Household Infrastructure)
3	Updated Historic Financial Assessment
4	Future Revenues
5	Affordable Future Capital Investment
6	Scenario Analysis
7	**Ratio Analysis**
8	Conclusions

Predicted Ratios

The Base Case predicted ratios are presented below. Although the model is not programmed to measure the ratios as required by National Treasury in all instances, it does provide comfort that the municipality is sustainable in future - on condition that it operates within the assumed benchmarks set in the financial plan.

RATIO	HEALTHY NORM	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23	2023/24	2024/25	2025/26
Liquidity Ratios											
Current Ratio	2 : 1	0.4 : 1	0.5 : 1	0.8 : 1	1.3 : 1	1.6 : 1	1.9 : 1	2.0 : 1	2.1 : 1	2.0 : 1	1.8 : 1
Quick Liquidity Ratio	2 : 1	0.0 : 1	0.0 : 1	0.1 : 1	0.5 : 1	0.8 : 1	1.1 : 1	1.3 : 1	1.4 : 1	1.3 : 1	1.2 : 1
Minimum Liquidity Level (or Cost Coverage)	1 : 1	-1.8 : 1	-1.2 : 1	-0.2 : 1	0.6 : 1	1.3 : 1	1.8 : 1	2.1 : 1	2.3 : 1	2.3 : 1	2.0 : 1
Overdraft to Total Income	0	12%	7%	1%	0%	0%	0%	0%	0%	0%	0%
Operational Ratios											
Accounting Surplus	>0	62	82	109	96	91	93	86	81	73	60
Cash Operating Surplus	>0	-28	92	110	113	112	112	111	111	110	110
Cash from Operations as a % of own Revenue		23%	27%	30%	25%	24%	22%	21%	19%	18%	17%
Repairs and Maintenance to PPE	7.0%	2%	2%	2%	2%	2%	2%	2%	2%	2%	3%
Debtors Payment Ratio (app.)	>95%	90%	90%	90%	90%	90%	90%	89%	89%	89%	89%
Staff Costs	25% - 40%	38%	38%	38%	38%	38%	38%	38%	38%	38%	38%
External Gearing Ratios											
External Loan Liability Paid Coverage Ratio	2 : 1	3.8 : 1	7.3 : 1	9.4 : 1	8.5 : 1	8.4 : 1	12.9 : 1	14.0 : 1	37.2 : 1	11.8 : 1	5.1 : 1
External Interest and Capital Paid to Total Expenditure	7.5%	4%	3%	2%	2%	2%	1%	1%	0%	1%	2%
External Gearing Ratio (or Debt as a % of Own Revenue) (incl Overdraft)	40.0%	24%	17%	8%	4%	3%	2%	1%	0%	4%	8%

1	Planning Process
2	Updated Perspectives (Demographic, Economic, Household Infrastructure)
3	Updated Historic Financial Assessment
4	Future Revenues
5	Affordable Future Capital Investment
6	Scenario Analysis
7	Ratio Analysis
8	**Conclusions**

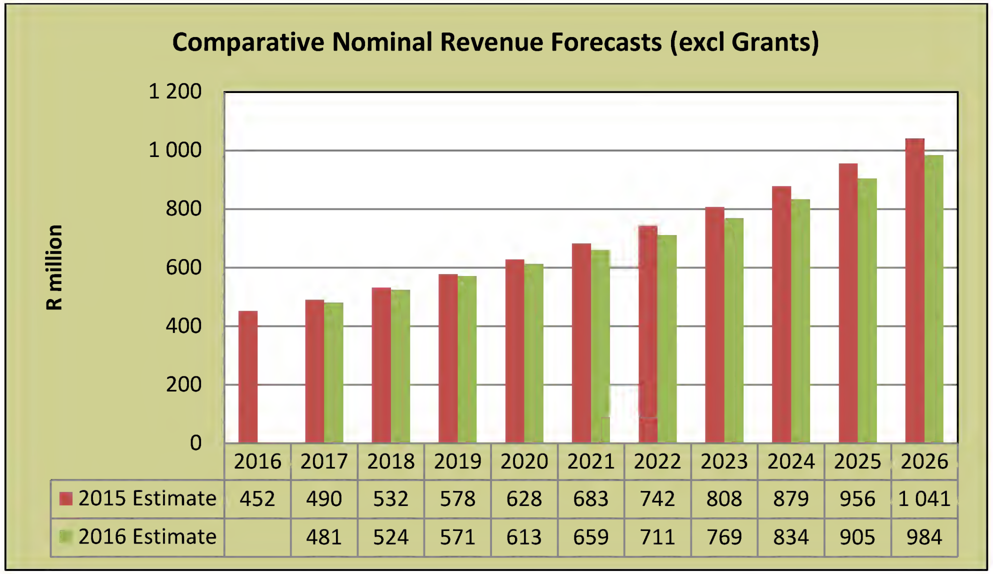
Conclusions

Revenues

The forecast Real Revenue per Capita exceeds the expected revenue per capita based on research done for municipalities with similar size economies and population sizes. Compared to a selection of municipalities in the Western Cape the household bill for a basket of services features close to the top end of those municipalities. Largely due to the low economic growth rate and high unemployment rate if compared to other municipalities in the district, the Municipal Revenue Risk Indicator (MRRI) is “High”.

We re-calibrated our model pursuant to the actual financial performance in 2016 and adjusted the Revenue expectation downwards from the estimates based on the 2015 performance. The variation of estimated Revenue (excluding Grants) across the two periods is within a range of 1% to 6%.

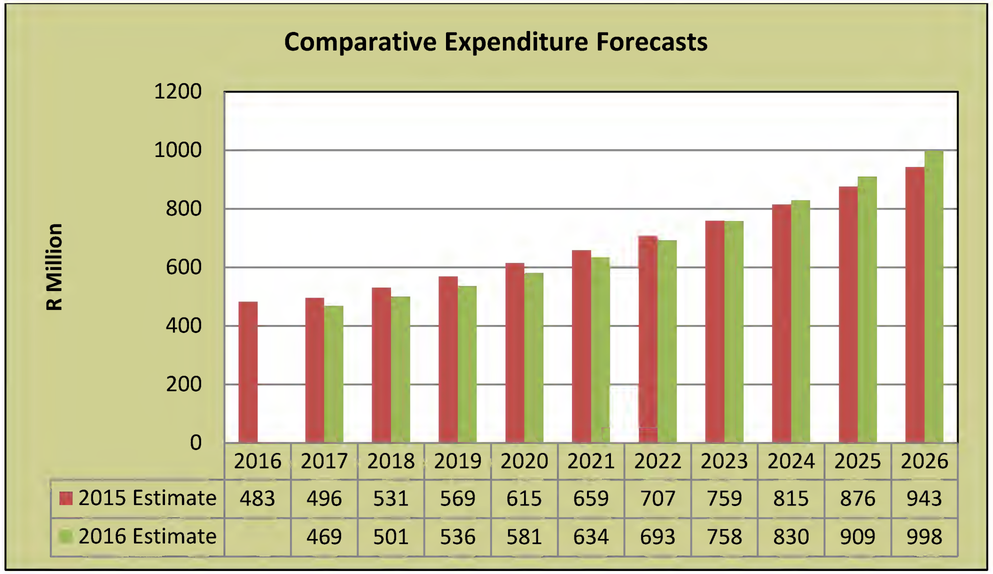
The economic development potential of the region must be harnessed to generate the expected revenues in future. Strategies to maintain and even improve the collection rates should also be implemented.



	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026
2015 Estimate	452	490	532	578	628	683	742	808	879	956	1 041
2016 Estimate		481	524	571	613	659	711	769	834	905	984

Expenditure

The estimated future expenditure patterns across the different years vary between 0% and 6%. The latest 2016 expenditure estimate is growing at a faster rate than the previous estimate.



	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026
2015 Estimate	483	496	531	569	615	659	707	759	815	876	943
2016 Estimate		469	501	536	581	634	693	758	830	909	998

Base Case

The Base Case Outcome for the 2015 and 2016 estimates are compared in the table below:

Description	2015 Estimate	2016 Estimate
Average annual % increase in Revenue	8.7%	10.5%
Surplus accumulated during 10 years Rm	394	481
10-year cash from operations after debt service Rm	418	184
10-year LT Debt Raised Rm	120	97
10-year capital investment programme Rm	895	859
Cash investments after 10 years Rm	208	166

The 10-year periods for the different estimates differ and it is difficult to make direct comparisons. Due to the proportionately higher operating expenses in the 2016 estimate, the capital investment also reduces slightly to R 859 million in the 10-year period.

Due to the incremental adjustments made each year on the model based on the latest financial, demographic and economic information we always place more reliance on the latest outcome, i.e. 2016 Estimate. In all instances the Cash Position at the end of the 10-year period is positive.

Funding Sources

It is estimated, based on the proportional growth of the indigent population and the initial unhealthy liquidity position of the municipality that the reliance on Capital Grants will dominate.

Source of Funding	2015 Estimate Rm		2016 Estimate Rm	
New Loans	R 120	13%	R 97	11%
Own Cash	R 38	4%	R 65	8%
Grants	R 572	64%	R 532	62%
Other	R 165	18%	R 165	19%
TOTAL	**R 895**	100%	**R 859**	100%

Note: The 10-Year periods differ for the four Estimates and can only provide an indication of changes among them.

Review of Recommendations made in 2015 (Based on the 2014 Estimate)

Refer to p. 56 – 62 of the *Oudtshoorn Long Term Financial Plan: 2016/17 – 2025/26*; July 2016. These recommendations were made in July 2016 and any achievements are not yet documented. They all remain relevant.

NO.	RECOMMENDATION	COMMENT
1	Implement the Organisation Restructuring	Remains relevant
2	Investigate Resort Management Options	Remains relevant
3	Ring Fence Cango Caves	Remains relevant
4	Investigate the Integrity of the Traffic Department	Remains relevant
5	Facilitate Local Economic Development	Remains relevant
6	Prepare a Comprehensive Municipal Infrastructure Plan	Remains relevant
7	Enhance Potential Revenue	Remains relevant
8	Improve Staff Productivity	Remains relevant.
9	Manage Overtime Effectively	Remains relevant
10	Align the Budget to Real Cash Flow	Remains relevant
11	Value for Money	Remains relevant
12	Involve Sports and Community Organisations	Remains relevant
13	Adopt a Municipal Viability Framework	Remains relevant
14	Implement integrated asset management	Remains relevant
15	Assess Condition of Assets	Remains relevant
16	Improve the Balance of the Capital Funding Mix	Remains relevant
17	Improve estimates of Future Capital Contributions	Remains relevant
18	Strengthen Credit Controls	Remains relevant

Concluding Remarks

1. The municipality continued to post Operating Accounting Deficits as well as Total Accounting Deficits over the eight year period. It is envisaged that this trend will change in future as there were substantial bad debt write-offs in FY2016.
2. The municipality achieved a high collection rate of 98% at FYE2016 and should endeavour maintaining it, as this is considered a healthy collection rate.
3. The declining liquidity position as reflected in the Current ratio of 0.37:1 at FYE 2016 is unusually low, due to the substantial increase of 111% in Payables and a simultaneous decrease of 49% in Consumer debtors. It had the effect however that the quality of the current assets improved and previously unaccounted creditors are now recorded.
4. The municipality's credit standing is still under pressure, due to the challenges experienced as a result of the interventions by COGTA, but it seems as if a turning point has been reached.
5. The growth trend in Gross Consumer debtors decreased by 20% at FYE 2016, due to the write-off of bad debts.
6. Gearing levels are low at 16%, but the scope to increase these levels at present, without a significant increase in revenue and operating cash to service the debt, is limited.
7. Further improvements to a Liquidity Reserve to fully cover all statutory requirements including 1 month of Opex is called for.
8. The municipality's improved cash position, is mainly due to a decrease of R141.48 million in Payments to Suppliers and employees, in the amount of R 343.55 million in FYE2016, from R 485.03 million in the previous year. The net result is that although a Net deficit of R22.13 million was experienced at FYE2016, the net movement in cash was a positive R67.28 million in FY2016, versus a negative movement of R60.34 million in 2016
9. The environment within which the municipality operates exhibits a "High" risk to generate own revenue. Little scope exists to increase Real Revenue per Capita through an above average increase of tariffs.
10. The 10-year capex demand far exceeds the affordability and the recommended integrated asset management system and comprehensive municipal infrastructure plan will serve the municipality well in optimising the application of its limited resources.
11. The precarious liquidity position of the municipality will prevent it from accessing external financing until FYE2025. Gearing levels in future remain well within the proposed benchmark of 30%.
12. We estimate that the municipality will be able to invest in a capital programme of R 859 million in the planning period to FYE2026 and be able to afford that 11% of this capex is funded with external financing.
13. The municipality has the potential to improve its financial position on condition that its finances are managed with care and discipline.

PROJECTED STATEMENTS

STATEMENT OF FINANCIAL PERFORMANCE	1	2	3	4	5	6	7	8	9	10
R '000 000	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23	2023/24	2024/25	2025/26
Revenue										
Property rates	71.15	78.41	86.17	93.84	102.29	111.60	121.86	133.20	145.72	159.56
Operational Grants Recognised	67.85	70.62	76.67	81.96	87.70	93.92	100.69	108.04	116.03	124.73
Income electricity services	225.14	249.84	276.97	301.62	328.76	358.68	391.68	428.10	468.35	512.84
Income water services	70.27	74.62	82.10	89.41	97.45	106.32	116.10	126.90	138.83	152.02
Agency Services	2.34	2.50	2.67	2.86	3.06	3.27	3.51	3.77	4.04	4.35
Other service charges and income	112.23	118.82	123.42	125.22	127.90	131.50	136.04	141.54	148.00	155.43
Total Revenue	548.99	594.82	648.00	694.90	747.16	805.30	869.88	941.54	1 020.97	1 108.93
Expenditure										
Salaries, wages and allowances	-201.59	-217.38	-232.37	-251.20	-274.19	-299.61	-327.73	-358.87	-393.39	-431.69
Expenditure electricity services	-150.01	-161.80	-174.52	-189.31	-206.64	-225.80	-246.99	-270.46	-296.47	-325.34
Expenditure water services	-0.32	-0.34	-0.36	-0.39	-0.43	-0.47	-0.51	-0.56	-0.62	-0.68
Repairs and maintenance	-13.45	-16.04	-16.74	-18.09	-19.75	-21.58	-23.61	-25.85	-28.34	-31.09
General expenses	-103.53	-105.00	-111.82	-121.73	-132.88	-145.19	-158.82	-173.91	-190.64	-209.20
Total Expenditure	-468.90	-500.56	-535.81	-580.74	-633.89	-692.65	-757.66	-829.65	-909.45	-997.99
EBITDA	80.09	94.26	112.19	114.17	113.27	112.65	112.22	111.89	111.52	110.93
Interest on Long Term Debt	-7.21	-6.21	-5.30	-4.30	-3.18	-1.95	-1.10	-0.42	-5.25	-12.35
Interest BB/[OD]	1.11	-9.19	-6.19	-1.25	1.87	4.06	6.35	8.26	10.33	11.23
Depreciation	-20.75	-22.14	-23.87	-25.15	-26.43	-27.86	-29.28	-30.64	-33.42	-36.80
Surplus/Deficit	**53.24**	**56.72**	**76.82**	**83.47**	**85.53**	**86.89**	**88.19**	**89.10**	**83.18**	**73.02**

STATEMENT OF FINANCIAL POSITION	1	2	3	4	5	6	7	8	9	10
R '000 000	**30-Jun-17**	**30-Jun-18**	**30-Jun-19**	**30-Jun-20**	**30-Jun-21**	**30-Jun-22**	**30-Jun-23**	**30-Jun-24**	**30-Jun-25**	**30-Jun-26**
Current Assets										
Receivables	54.06	58.57	63.81	68.42	73.57	79.29	85.65	92.71	100.53	109.19
Investment for Liquidity	0.00	0.00	0.00	31.24	66.57	102.37	116.86	140.29	150.71	154.90
Investment for CRR	0.00	0.00	0.00	0.00	0.00	0.00	14.29	21.17	22.05	11.02
Other Encumbered Investments	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Cash in Bank	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Non-Current Assets										
Property Plant & Equipment	711.89	759.78	819.06	862.95	906.97	955.91	1 004.62	1 051.14	1 146.68	1 262.62
Investment Property	76.62	76.62	76.62	76.62	76.62	76.62	76.62	76.62	76.62	76.62
Total Assets	**842.56**	**894.97**	**959.49**	**1 039.23**	**1 123.73**	**1 214.19**	**1 298.05**	**1 381.93**	**1 496.59**	**1 614.35**
Current Liabilities										
Creditors	38.54	41.14	44.04	47.73	52.10	56.93	62.27	68.19	74.75	82.03
Bank Overdraft	72.37	48.37	9.65	0.00	0.00	0.00	0.00	0.00	0.00	0.00
ST Non-Interest Bearing Liabilities	20.02	22.96	26.35	30.27	34.80	40.04	46.12	53.16	61.34	70.83
Non-Current Liabilities										
LT Interest Bearing Liabilities	58.14	50.03	41.09	31.17	20.33	12.92	5.77	3.21	38.50	89.42
LT Non-Interest Bearing Liabilities	111.62	127.99	146.90	168.75	194.01	223.26	257.13	296.40	341.96	394.87
Accumulated Surplus & Reserves	541.88	604.48	691.46	761.31	822.49	881.05	926.76	960.97	980.04	977.20
Total Liabilities	**842.56**	**894.97**	**959.49**	**1 039.23**	**1 123.73**	**1 214.19**	**1 298.05**	**1 381.93**	**1 496.59**	**1 614.35**

CASH FLOW STATEMENT	1	2	3	4	5	6	7	8	9	10
R '000 000	**2016/17**	**2017/18**	**2018/19**	**2019/20**	**2020/21**	**2021/22**	**2022/23**	**2023/24**	**2024/25**	**2025/26**
Cash In										
Surplus / [Deficit]	53.24	56.72	76.82	83.47	85.53	86.89	88.19	89.10	83.18	73.02
Add Depreciation	20.75	22.14	23.87	25.15	26.43	27.86	29.28	30.64	33.42	36.80
Deduct Impairment	-38.46	-41.85	-48.37	-51.89	-59.01	-63.65	-72.53	-78.58	-89.67	-97.50
Proceeds from Sale of Assets	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Capital Grants	42.55	57.04	70.83	49.04	49.46	49.80	50.00	50.01	54.30	59.05
Other Capital Contributions	5.00	10.00	10.00	15.00	15.00	20.00	20.00	20.00	25.00	25.00
LT Debt Raised	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	39.08	57.66
Total Cash In	**83.07**	**104.06**	**133.15**	**120.77**	**117.41**	**120.90**	**114.94**	**111.16**	**145.30**	**154.02**
Cash Out										
Invest in PPE	-52.36	-70.04	-83.15	-69.04	-70.46	-76.80	-78.00	-77.15	-128.96	-152.73
Invest in Cash Backed Reserves	0.00	0.00	0.00	-36.24	-36.34	-36.80	-29.78	-22.30	-18.47	-3.79
Working Capital	-108.31	-1.91	-2.34	-0.93	-0.78	-0.90	-1.02	-1.14	-1.26	-1.38
LT Debt Repaid	-14.53	-8.11	-8.94	-9.92	-10.83	-7.41	-7.15	-2.57	-3.78	-6.74
Total Cash Out	**-175.20**	**-80.06**	**-94.43**	**-116.12**	**-118.41**	**-121.90**	**-115.94**	**-103.16**	**-152.47**	**-164.65**